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DEPARTMENT OF STATE

Memorandum of Conversation

DATE: March 7, 1961

SUBJECT: Volta River Project: VALCO Financ..

PARTICIPANTS:

DEPARTMENT OF STATE A/GIS/NR
REVIEWED BY RS DATE MAY 1982
PORTIONS EXCISED AS NOTED

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Participants

Mr. Chad Calhoun, Vice President, Kaiser Industries
Mr. Lloyd Cutler, Attorney for the Aluminum companies
Mr. Ronald Sullivan, Attorney, Sullivan & Cromwell
Mr. Sam Stern, Attorney, Sullivan & Cromwell

State

Mr. Abram Chayes, Legal Adviser
Mr. Peyton Kerr, Deputy Assistant Secretary for Economic Affairs
Mr. Charles Warden, Chief, Investment Guaranties Division, ICA
Mr. Dean Lewis, Legal Staff, ICA
Mr. Glenn McLaughlin, Eximbank Staff
Mr. George Kenney, OFD/ED

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~~COPIES TO:~~ Mr. Glenn McLaughlin, Eximbank Staff
Mr. George Kenney, OFD/ED

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545J.2614/3-761

Mr. Calhoun summarized the companies' position with regard to the main points of the Government proposal. First, with regard to the request for $40 million in equity capital, the companies' agreement with Ghana provides for an equity of $32 million annually on the total investment of $178 million. He implied that the companies would be prepared to apply the $32 million in either equity or stockholders' advances on the 4-pot line smelter valued at $123 million. That would be an equity of 25%. Second, with regard to the debt proposal for a 50-50 split between private and government loan capital, the companies feel that there is no time in which to obtain money from private lenders and that a full government loan for $96 million will be required. Third, on the guarantees, the companies would be willing to accept a DLF guarantee on the equity of 90% with certain specified exceptions to the coverage. As a fee for this guarantee the DLF would receive a per cent of VALCO profits.

[redacted]

A memorandum summarizing the above points was submitted by Mr. Calhoun.

Mr. Cutler stated that the financial experts of the companies claimed it would take too long to work out loan agreements or commitments with private lenders if the Government guarantees are no better than the previous offer.

Another

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Another problem is that lenders will not commit funds five years in advance without charging some interest. This would be a considerable increase in cost, for the companies will not need the money until 1965. One pot line at a time will be completed and the company plans to build the smelter so that it can be completed approximately at the same time that power becomes available. He explained that the Ghana Government did not want to be firmly committed to supply electric power on January 1, 1967. Therefore, the companies were given an option regarding the timing of their construction within a limit of two years following completion of the dam.

Mr. Chayes pointed out that if the Government provides so much capital the companies will be taking no risk except, of course, buying the power and the aluminum ingot production which is in effect the same commitment. Therefore the risk is one of marketing the product. Mr. Cutler disagreed by saying the company plans to build facilities in Louisiana to produce alumina from Surinam bauxite. In addition the companies are putting up 25% of the equity, and the commitment to purchase aluminum output goes beyond the normal commitments of the companies. There is a difference between this kind of operation and a domestic one in that as an operating company in the latter case they do not guarantee to buy ingots from their own plants nor to buy power over a long period of time from local power companies - although they may have to pay some curtailment charges. [redacted] B1

Mr. Chayes commented that he saw little difference between the proposed arrangement and a management contract. What risk would the companies really be taking? For example, when they invest in the United States the risks are much greater than purely marketing risks. In Ghana, however, we have agreed that the companies are entitled to broad protection against abnormal risks, but as the proposal is now being presented the residual risks for the companies would be even smaller on the entrepeneurial side than with a U.S. investment. The companies simply did not agree with this analysis and continued to maintain that their guarantee of a market for this particular smelter places the output of that smelter on a priority basis for marketing purposes in comparison with their other plants. They would not say exactly where the Ghana smelter would rank in terms of cost but mentioned that present capacity of Kaiser aluminum is 600,000 tons per year and the capacity of the Ghana plant would add 120,000 tons annually. (Note: Sales of Kaiser Aluminum have grown at an annual rate of over 10% for the past five years. Thus the new plant would add about two years sales growth to capacity, assuming a steady growth in demand for aluminum.) Mr. Cutler said the investment in Ghana is economically

feasible

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feasible and financially attractive provided the risks can be reduced. The commitment to buy electric power even when not needed effectively raises the cost to 3 mills per kwh. Of course, if the Boke project is completed, then alumina imported from Guinea would be much cheaper than that from the United States. On the financing side he added that the companies are really indifferent about private versus public money if the Government is able to give appropriate guarantees in time to arrange financing. The risk is greater on equity because of the priority given to the plant. However, the companies think they can live with this commitment.

There was more discussion of the problem of establishing patterns as a result of such a large share of government participation in what is essentially a private operation, and in this case going beyond what the Government is doing for the dam which is public. Mr. Calhoun made mention of the Turkish steel mill financing arrangements, but this analogy was not considered apt. Mr. Chayes emphasized that a policy matter was involved and that a decision must be made with the realization that we <u>are</u> setting a pattern, especially if guarantees are used, and at the same time we must remain within statutory limits.

Mr. Cutler thought that the normal risks would be definable. Mr. Chayes reflected on the nature of the cooperation between the Government and the companies and said it appeared to be that Government participation was on a fee basis rather than on the basis of a share in ownership. This was explored with regard to the rationale of the equity participation and Mr. Cutler analyzed the company costs in terms of opportunity costs, management services and marketing risks in such a way that Mr. Chayes was led to observe that the company share in profits would be roughly equivalent to a management fee plus interest on invested capital plus a return on the market risk. Mr. Cutler agreed and said that the company proposal did not suggest any flat fees but did not mean to exclude such a possibility.

Concerning the timing problem the group was reminded that bids had been opened on February 16 and that contracts on construction should be awarded by April 17. Some work must be done before November, otherwise there would be considerable delay in construction. According to Mr. Calhoun, Kaiser Engineers, which is the firm analyzing bids for the Ghana Government, has not decided to ask for any revision of bids nor to delay the established deadline, although there may be some slippage. The bids in fact are quite favorable with respect to earlier estimates.

With regard to financing for the dam, the requirements which had to be met in order to satisfy the World Bank were reviewed. Mr. Cutler said this consisted mainly of the signing of a firm power contract by VALCO and the validation of VALCO's agreement with Ghana. If there is a financing problem, the bids are written so that Ghana can award a contract and terminate it after three months, but this is a risky procedure.

Regarding

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As the meeting drew to a close there was a return to a discussion of the requirements for U.S. government financing. Mr. Cutler emphasized that a loan of $96,000,000 was needed because the companies are not sure that the government can make the kind of guarantees that are necessary, but he added that they had always wanted more private money. The insurance companies want a guarantee of payment from people they can trust. Mr. Warden said their proposal was written in such a way that normal business risks in Ghana were equated with political risks. Therefore there is no normal risk left except the market. Continuing on this line, Mr. Chayes said that fluctuations in tax rates in the United States and other administrative risks could be greater than in Ghana under the contemplated arrangements. He could see normal cuts by a responsible administration in Ghana which would make the smelter operations less profitable. Therefore we cannot conclude that everything the Government of Ghana might do would represent an abnormal risk. Mr. Cutler thought rather in terms of the contractual arrangements, since acts of the Ghana Government would not affect all aluminum procedures but just VALCO. He assumes the U.S. and Ghanaians will have an agreement.

Mr. Chayes said he thought the option which the companies wanted either to charge for current damages or to dump the operation was asking too much. Mr. Cutler replied that the companies would be willing to give the Government the option of accepting a partial claim or asking the companies to withdraw it and give up their operation.

The next meeting was not fixed but Mr. George Woods, financial advisor to VALCO will be in Washington on Friday. The companies would like an earlier meeting if possible.

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